Determinants of Firm Value and Earnings Management in Indonesian Sharia Stock Companies

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The objective of the research was to analyse the impact of Good Corporate Governance (GCG) (institutional ownership, independent commissioners, audit committees), profitability, financial leverage, and firm size on firm value, with earnings management as a moderating variable. Data are collected from the financial statements of manufacturing companies listed in ISSI in the period of 2014-2018. The result showed that, GCG (institutional ownership, independent commissioners, audit committee), profitability, financial leverage, and firm size significantly influenced firm value. Institutional ownership did not have any influence on firm value. Audit committees negatively influenced firm value. Independent commissioners, profitability, financial leverage, and firm size positively influenced firm value. Earnings management as a moderating variable could not moderate the correlation of GCG (institutional ownership, independent commissioners, audit committee), profitability, financial leverage, and firm size on firm value.

Key words: *Good Corporate Governance, Profitability, Financial Leverage, Firm Value, and Earnings Management.*

Introduction

Firm value (Gitman, 2006) is an actual value per share that will be received if a company sold its asset at its market price. The selling value that exceeds the liquidation value is considered as the value of the management organisation that runs a company (Sartono, 2010). Instead of measuring stock price, firm value can be reflected in Tobin's Q ratio. Tobin's Q ratio is an indicator of firm value that shows management's performance in managing its assets and the potential market value of a company (Dushnitsky and Lenox, 2006). PT. Multi Sarana Aranda (MASA) suffered a loss in 2017, but the market price of stocks per share and the value of Tobin's Q have actually increased. The aforementioned phenomenon shows that changes in firm value are not reflected in stock prices or net income. This is certainly

contrary to theory. In addition, in 2016, PT Timah Persero was suspected of reporting fictitious financial statements in the first quarter (Q1) of 2015. Management stated that the company made a profit every year. However, *Ikatan Kerja Timah* (IKT) revealed that the company suffered losses for 3 (three) consecutive years since 2013 (Cahyadi and Mertha, 2019). According to Mahirun and Andi (2018), the increase in firm value is its own achievement for investors, because firm value follows the level of stakeholder welfare. A manager's decision also affects the optimal results to increase firm value, so the manager has an important role which relates to whether there is an indication of earnings management in a company. Therefore, this phenomenon becomes the background of the research problem.

Literature Review

Agency Theory

Differences in interests lead to a shift in risk sharing (Bendickson, 2016), where the principal will have more risks if the agent acts on the basis of self-interest or intrinsic egoism (Kultys, 2016) to produce agency conflict. Agency conflict arises because each individual prioritises their own benefit, so that each individual will try to maximise their interests and cause information asymmetry. Information asymmetry is the difference in information held by each of the principal and agent (Safriliana et al., 2019); an imbalance.

Management manages and controls the company more than the shareholders do, so the agent obtains internal information more widely than other stakeholders. Agents can use their information asymmetry to hide some information related to the presentation of financial performance, and maximise their interests in the form of earnings management (Siahaan, 2017). Agency theory addresses the problem of differences in interests between principal and agent. Thus, agency theory underlies the relationship between principal, agent and firm value.

Signalling Theory

Shareholders who invest their funds in a company cannot ensure the value of a company in the future (future value). Therefore, they depend on the 'signal' to reduce uncertainty regarding the company's future performance. A signal can be in the form of information (Zurriah, 2016) about what management has done to fulfil shareholders' expectations. Signals can also be in the form of promotions or other information stating that one company is better than another company.

Connelly et al. (2011) show 2 (two) situations involving information asymmetry where signalling theory is enforced, namely: (1) cases where information asymmetry occurs between two parties, one party is able to limit the other party's ability to judge a value or

quality against another value or quality; and (2) cases where information asymmetry limits one party's understanding of the expected behaviour or intent of another behaviour. Thus, signalling theory is closely related to stakeholders and corporate values.

Firm Value

One of the company's targets is to maximise its value. According to firm theory (the theory of the firm) its main target is to maximise its wealth or value (Sartono, 2009 and Muda et al., 2018) through the rise of share price. By maximising firm value, management has been responsible to shareholders and succeeded in prospering the stakeholders. According to Harmono (2009), the value of a firm is the company's performance which is reflected in the share price, as formed by the demand and supply of the capital market which reflects the public's judgment or perception of the company's performance. Therefore, managers must decide on effective strategies and steps (Mahirun and Andi, 2018) to optimise company value.

Good Corporate Governance (GCG)

Agency conflicts and earnings management actions can be detrimental to stakeholders, especially shareholders. Both can be overcome by implementing GCG. GCG is considered as a tool that limits managers' interests, to pursue shareholders' interests (Kultys, 2016), to increase the firm's value.

Institutional Ownership

Institutional ownership is the inclusion of shares owned by external stakeholders other than managerial ownership. As defined by Yang et al. (2009), institutional ownership is shares of companies owned by an institution, such as insurance companies, financial institutions (banks, financial companies, credit), pension funds, investment banking and other companies related to this category.

Independent Commissioner

Independent commissioners are members of the board of commissioners who do not have share ownership in the company and / or are associated with one member of the board of commissioners who can influence their attitude in acting independently (Zulfikar et al., 2017). Independent commissioners are an important part of the corporate governance mechanism that functions to oversee and control conflicts of interest between controlling shareholders and minority shareholders, which can lead to inefficiencies in company management.

Audit Committee

The audit committee has a duty to maintain and improve the quality of financial reports, so that the reports produced are reliable and trustworthy. The roles and tasks related to the audit committee (Fauzi et al., 2017) are: (1) assessing the implementation of activities and audit results carried out by internal and external auditors in preventing implementation and reporting that does not meet the standards; (2) recommending matters related to improving the company's management control system and its implementation; (3) ensuring a satisfactory review procedure for information issued by state-owned enterprises (BUMN); and (4) performing other tasks given by the commissioner or supervisory board.

Profitability

Profitability measures a company's operational performance as reflected in its profits. Many stakeholders measure company performance as based on financial statements. This idea is called profit-oriented stakeholders (Putu et al., 2014). Megawati (2010) defines profitability as the company's ability to generate profits. ROA is a comprehensive measurement indicator and is superior compared to other measurement indicators, because it is useful to see the condition of a company based on the financial statements presented (Ikhwal, 2016).

Financial Leverage

High financial leverage will reduce company value, along with the increased company risk of failure to pay off the debts (Obradovich and Amarjit, 2013). Financial leverage can be measured by debt ratio. Cuong and Canh (2012) found that the optimal debt ratio (total debt to total assets ratio) should not exceed 59.27%, and valuing the ratio more than this limit will negatively affect company value.

Firm Size

The size of the firm can be seen from the high or low price of shares sold on the capital market. As stated by Issar (2017), firm size is based on the size or proportion of the company's stock price, multiplied by the number of shares outstanding or market capitalisation of the market of other companies.

Earnings Management

The term of earnings management can be associated with management's efforts to calculate and determine earnings according to their wishes. In accounting theory, profit is the excess income earned by a company after deducting a number of expenses, and one of the principles

governed is the accrual principle (Muda et al., 2018b). Based on this principle, a company can manage profits by increasing or decreasing profit in a certain year. Therefore, earnings management is the regulation of excess corporate earnings, in accordance with the principles allowed by the regulatory board to achieve certain goals.

Research Framework

The research framework is presented in Figure 1 as follows:

Figure 1. Research Framework
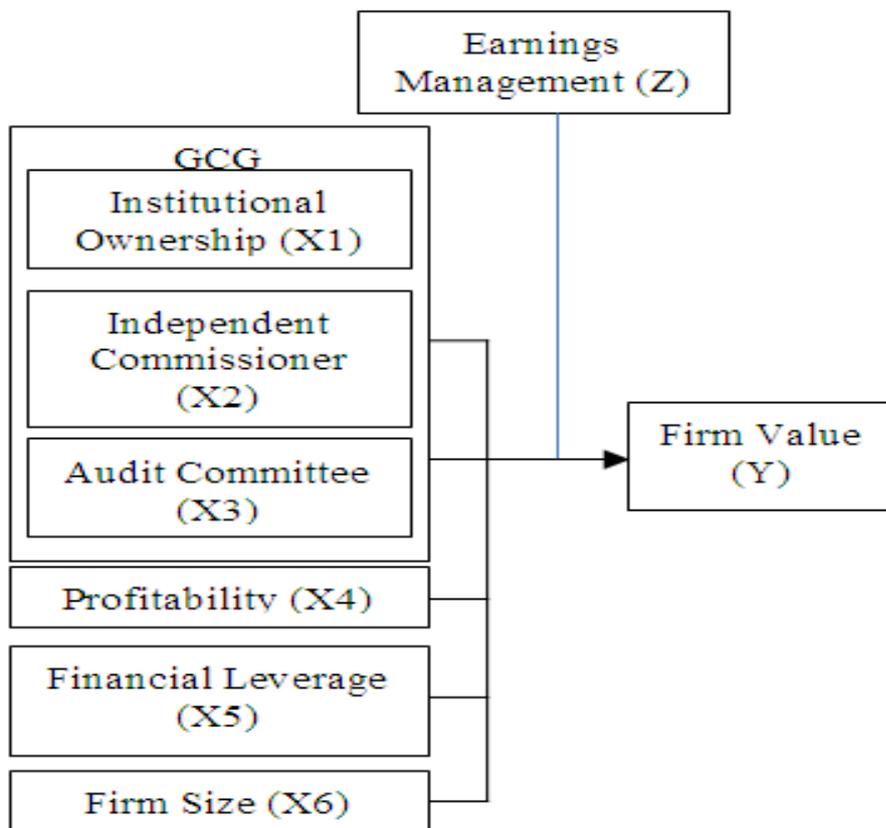
The research hypothesis is as follows:

H_1: Institutional ownership has a positive effect on company value.
H_2: Independent commissioners have a positive effect on company value.
H_3: Audit committee has a positive effect on company value.
H_4: Profitability has a positive effect on firm value.
H_5: Financial leverage has a positive effect on firm value.
H_6: Firm size has a positive effect on firm value.

H$_7$: Earnings management can moderate the influence of good corporate governance (institutional ownership, independent commissioners and audit committees), profitability, financial leverage and company size on firm value.

Research Methods

The research design used as a reference for research strategies to answer research questions is causal associative. Causal associative research relates a variable to other variables. The population in this study is companies included in the manufacturing subsector which are listed on the Indonesia Shariah Stock Index (ISSI), in the period 2014-2018; a total of 153 companies. By using purposive sampling, 25 companies were chosen. As the period of study is five year, it became 125 observations. This secondary data is collected from published annual reports accessed via the internet (www.idx.co.id) in 2014-2018.

Operational Definitions

Table 1: Operational Definitions

Variable	Operational Definition	Indicator	Scale
Firm Value	Firm value is a perception of the people, especially the stakeholders, about the success or failure of a company in maximising the welfare of stakeholders.	$Q = \dfrac{MVC+AVD}{AVA}$	Ratio
Institutional Ownership	Institutional ownership is the percentage of share ownership owned by external parties such as financial institutions (banks, insurance companies) and or shareholders.	**Institutional Ownership =** $\dfrac{\text{Institutional Shares}}{\text{Outstanding Shares}}$ **x 100%**	Ratio
Independent Commissioner	The independent commissioner functions to control and oversee the process of the company's business activities independently, impartially and does not have an interest which becomes a liaison or mediator for the company's managers and shareholders.	**Independent Commissioner =** $\dfrac{\text{Independent Commissioner}}{\text{Total Independent Comissioner}}$ **x 100%**	Ratio

Audit Committee	Audit committee maintains the quality of the financial statements to remain reliable and trustworthy. Audit committee is expected to be able to assess the company's performance presented by internal and external auditors and recommend better control tools for the company.	**Total Audit Committee**	Nominal
Profitability	Profitability is a ratio used to measure the success of a company in managing assets and capital so as to produce returns in the form of income or profits.	$ROA = \frac{Net\ Income}{Total\ Asset}$ **x 100%**	Ratio
Financial Leverage	Financial leverage is a funding decision taken by management in order to finance the company's operational activities by utilising additional funds sourced from external parties, namely banks.	$DAR = \frac{Total\ Debt}{Total\ Asset}$ **x 100%**	Ratio
Firm Size	Firm size is a reflection of the number of assets and capital owned by a company. Firm size is classified into small, medium and large.	**Size = Ln total asset**	Ratio
Earnings Management	Earnings management is a process of managing earnings performed by managers on personal interests related to financial reporting to improve the quality of reports to external parties.	$\Delta AR it = \alpha + \beta 1\ \Delta R1\_3 it + \beta 2\ \Delta R4 it + e$	Ratio

Data Analysis Technique

Data analysis technique used in this study is multiple linear regression analysis with moderating variables through residual test testing. The equation of multiple linear regression analysis is as follows:

$$Y = \alpha + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \beta_4 X_4 + \beta_5 X_5 + \beta_6 X_6 + e$$

Information:
Y: Firm Value
α: Constants
β1 - β6: Regression Coefficient
X1: Institutional Ownership
X2: Independent Commissioner
X3: Audit Committee
X4: Profitability
X5: Financial Leverage
X6: Firm Size
e: Error

For testing moderating variables with residual tests, the regression equation is as follows:
$$Z = \alpha + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \beta_4 X_4 + \beta_5 X_5 + \beta_6 X_6 + e \ldots\ldots .. (1)$$
$$|\varepsilon| = \alpha + \beta_7 Y \ldots\ldots\ldots ... \ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots .. (2)$$

Information:
Y: Firm Value
α: Constants
β1 - β7: Regression Coefficient
X1: Institutional Ownership
X2: Independent Commissioner
X3: Audit Committee
X4: Profitability
X5: Financial Leverage
X6: Firm Size
Z: Profit Management
e: Error

Results and Discussions

Result

Data Descriptive

Data descriptions are presented in the following Table 2:

Table 2: Data Descriptive

	N	Min.	Max.	Mean		Std. Deviation
Firm Value (Y)	125	.57	23.29	2.67	.33	3.72277
Institutional Ownership (X1)	125	.00	1.00	.88	.02	.29507
Independent Commissioner (X2)	125	.14	.80	.37	.01	.11824
Audit Committee (X3)	125	3	5	3.15	.03	.382
ROA (X4)	125	-5.88	46.66	9.14	.81	9.14320
DAR (X5)	125	.07	.73	.36	.01	.16784
Firm Size (X6)	125	25.88	33.47	28.96	.16	1.82193
Earnings Management (Z)	125	-1.67	7.23	.00	.08	.99190
Valid N (list wise)	125					

Source: processed by Author (2019).

The results of descriptive statistical analysis show in Table 2 above. The results of the data analysis, including the test of normality, multi-collinearity test, heteroscedasticity test, and the test of autocorrelation, show that the data are free from those symptoms.

Hypothesis Testing

Coefficient of Determination (R^2)

Table 3: Determination Coefficient Test Results (R^2)

Model Summary[b]			
Model	R	R Square	Adjusted R Square
1	.897[a]	.805	.795

a. Predictors: (Constant), X1-X6
b. Dependent Variable: Firm Value (Y)
Source: processed by Author (2019).

The adjusted value (R^2) is 0.795 or 79.5%. That is, institutional ownership variables (X1), independent commissioners (X2), audit committee (X3), probability (X4), financial leverage (X5), company size (X6), and earnings management (Z) are able to explain the dependent variable, namely it values company (Y) at 79.5%; while the remaining 20.5% is explained by other variables or factors.

F Statistic Test (Simultaneous Test)

Table 4: F Statistic Test Results

ANOVA[b]					
Model	Sum of Squares	df	Mean Square	F	Sig.
1 Regression	1382.674	6	230.446	80.967	.000[a]
Residual	335.846	118	2.846		
Total	1718.520	124			

a. Predictors: (Constant), X1-X6
b. Dependent Variable: Firm Value (Y)
Source: processed by Author (2019).

The significance value is smaller than 0.05 (0,000 <0.05). Thus, institutional ownership variable (X1), independent commissioner (X2), audit committee (X3), probability (X4), financial leverage (X5), company size (X6), and earnings management (Z) simultaneously influence the firm value (Y).

t Statistic Test (Partial Test)

Table 5: t Statistics Test Results

Coefficients[a]					
	UC		SC		
Model	B	Std. Error	Beta	t	Sig.
1 (Constant)	-7.334	2.780		-2.638	.009
Institutional Ownership (X1)	-1.023	.564	-.081	-1.814	.072
Independent Commissioner (X2)	7.147	1.645	.227	4.343	.000
Audit Committee (X3)	-1.298	.458	-.133	-2.833	.005
ROA (X4)	.269	.022	.660	12.437	.000
DAR (X5)	8.698	.988	.392	8.806	.000
Firm Size (X6)	.231	.095	.113	2.420	.017

a. Dependent Variable: Firm Value (Y).
Source: processed by Author (2019).

The regression equation based on the results of the t statistic test is as follows:

Y = -7,334 - 1,023X1 + 7,147X2 - 1,298X3 + 0,269X4 + 8,698X5 + 0,231X6

Based on Table 9, the significance and influence of each variable are as follows:

a. Institutional ownership (X1) (0.072> 0.05) does not affect the firm value (Y).
b. Independent commissioner (X2) (0,000 <0.05) has a positive effect on firm value (Y).
c. Audit committee (X3) (0.005 <0.05) has a negative effect on firm value (Y).
d. Profitability (X4) (0,000 <0.05) has a positive effect on firm value (Y).
e. Financial leverage (X5) (0,000 <0.05) has a positive effect on firm value (Y).
f. Company size (X6) (0.017 <0.05) has a positive effect on firm value (Y).

Moderating Variable Hypothesis Test

The results of the calculation of earnings management with the Stubben model (2010) show the residual value of each company that is indicated or does not manage earnings. Earnings management value is classified by limiting the residual value of -0.075 to 0.075, which indicates that a company has not indicated earnings management (Sari and Nurmala, 2014). In research Roychowdhurry (2006) states that the limits for companies not indicating earnings management have a residual value close to 0.

Table 6: Earnings Management (EM) Classification

No.	Classification	Description	Years					Total
			2014	2015	2016	2017	2018	
1.	< -0,075	Indicate EM	20	19	24	14	15	92
2.	-0,075 to 0,075	Not Indicate EM	3	3	0	4	7	17
3.	> 0,075	Indicate EM	2	3	1	7	3	16
Total			25	25	25	25	25	125

Source: Author's tabulation (2019).

Based on Table 6 above, the companies indicating earnings management in 2014 and 2015 were 22 companies, out of a total of 25 companies. In 2016, 25 companies indicated earnings management, as did 21 companies in 2017, and 18 companies in 2018. Three companies were not indicating earnings management in 2014 and 2015, while zero did in 2016, as did four in 2017, and seven in 2018. Thus, the company's residual value which is not indicated by earnings management is eliminated from research observational data, to test the effect of moderation by residual testing.

Table 7: Residual Test Results on Earnings Management

Coefficientsᵃ

Model		UC		SC		
		B	Std. Error	Beta	t	Sig.
1	(Constant)	-6.119	1.744		-3.509	.001
	Institutional Ownership (X1)	.288	.357	.082	.807	.422
	Independent Commissioner (X2)	.236	1.046	.026	.225	.822
	Audit Committee (X3)	.689	.304	.246	2.270	.025
	ROA (X4)	-4.051	.014	.000	-.003	.998
	DAR (X5)	-.169	.643	-.027	-.264	.793
	Firm Size (X6)	.127	.063	.223	2.035	.044

a. Dependent Variable: Earnings Management (Z)
Source: proceed by Author (2019).

Table 8: Residual Value Test Results (Abs_Res1)

Coefficientsᵃ

Model		UC		SC		
		B	Std. Error	Beta	t	Sig.
1	(Constant)	.486	.103		4.707	.000
	Firm Value (Y)	-.006	.023	-.024	-.250	.803

a. Dependent Variable: Abs_Res3
Source: proceed by Author (2019).

Based on Tables 7 and 8, the 2 (two) regression equation models are as follows.

$Z = -6,119 + 0,288X1 + 0,236X2 + 0,689X3 - 4,051X4 - 0,169X5 + 0,127X6...(1)$
$| \varepsilon | = 0,486 - 0,006Y$ …………………………………………………… ...... (2)

In the second regression model, the significance value is greater than 0.05 (0.803> 0.05). Therefore earnings management (Z) is not a moderating variable that can strengthen or weaken the relationship between institutional ownership (X1), independent commissioner (X2), audit committee (X3), probability (X4), financial leverage (X5), and company size (X6) on firm value (Y).

Discussion

Based on the results of the partial research conducted, the interpretation of each independent variable is as follows:

Effect of Institutional Ownership on Firm Value

The existence of ownership by the institution can provide monitoring from external parties, so that management will try to improve the performance and increase firm value. But the results of the study showed that high institutional ownership actually lowered the value of a company. This can be caused by the existence of a hypothesis regarding the effect of institutional ownership on firm value, namely the efficiency abatement hypothesis (Pound, 1988); where shareholders monitor a company passively and do not prioritise company performance. Thus, institutional ownership cannot affect firm value at all. The results of this study are consistent with research conducted by Silitonga (2012), Zurriah (2016) and Muda (2018b) which states that institutional ownership has no effect on firm value.

The Influence of Independent Commissioners on Firm Value

The presence of an independent commissioner can minimise agency costs that may arise due to differences in interests between shareholders (El-Chaarani, 2014) and prevent fraud from the manager that can affect shareholder welfare (Dahliwal, 2007). The results of this study are not consistent with the researches of Hariani (2012) and Rosari (2015), which state that independent commissioners have no significant effect on firm value.

The Influence of the Audit Committee on Firm Value

The audit committee has a role to maintain and improve the quality of financial statements so that the reports produced are reliable and trustworthy. Based on empirical results, the audit committee is a factor that influences firm value, but the audit committee is considered not yet fully effective in monitoring the company internally. That is despite it meeting the Blue Ribbon Committee standards which require a minimum number of audit committees of 3 (three) people. The results of this study are consistent with research by Obradovich and Amarjit (2013) and Fauzi et al., (2017), which states that the audit committee has a significant effect on firm value. But other opinions such as Silitonga (2012) found that the audit committee had no significant effect on firm value.

Effect of Probability on Firm Value

Stakeholders assume that the success or failure of the company in facilitating management is assessed by analysing the performance of earnings or profitability. An increase in profit shows an increase in firm value. According to Modigliani and Miller (Brigham, 1999) firm value is determined by the level of profitability. The higher the profitability ratio, the higher the firm value. Therefore, high performance is supported by high ROA as well. The results of this study are consistent with Hariani (2012), Obradovich and Amarjit (2013), Putu et al., (2014), and Rini (2016) which state that profitability has a significant effect on firm value.

The Effect of Financial Leverage on Firm Value

Injections of external funds in the form of debt (debt) can overcome agency problems between managers and shareholders or creditors (Jensen, 1986). According to trade-off theory (Modigliani and Miller, 1963) debt can increase firm value, but on the other hand debt increases financial distress in the future. The higher the debt the greater the risk of default on a company (Shyam-Sunder and Myers, 1999). The results of this study are consistent with researches by Obradovich and Amarjit (2013), Rosari (2015), Mahirun and Andi (2018) which state that financial leverage has a significant effect on firm value. However, several research results such as Hariani (2012), Rini (2016), and Zuriah (2016) prove that financial leverage is not a factor that can affect firm value.

Effect of Firm Size on Firm Value

Firm size is based on the high and low prices of shares traded on the capital market (Issar, 2017). Large companies get more public attention, especially from the government and politicians, so they tend to maintain their image and reputation by improving the quality of financial reports and hiring the best managers (Marsh, 1982), increasing firm value. The results of this study are consistent with research by Obradovich and Amarjit (2013), Putu et al., (2014), Rosari (2015), Rini (2016), and Zurriah (2016) which states that firm size influences firm value. However, Hariani's research (2012), and Mahirun and Andi (2018) found that firm size had no effect on firm value.

Earnings Management in Moderating the Effects of Good Corporate Governance (Institutional Ownership, Independent Commissioners and Audit Committees), Probability, Financial Leverage, and Firm Size on Firm Value

The existence of a company that is indicated as performing earnings management does not increase firm value. This is in accordance with Scott's (2000) theory of opportunistic earnings management. Earnings management occurs because of certain motivations from managers

who want to maximise their interests and ignore company responsibilities to shareholders, by managing and applying earnings management.

Conclusion

Conclusion

Based on the results of the described research and discussion, there are several conclusions:
1. Institutional ownership does not affect firm value.
2. Independent commissioners have a significant and positive influence on firm value.
3. The audit committee has a significant and negative effect on firm value.
4. Profitability has a significant and positive effect on firm value.
5. Financial leverage has a significant and positive effect on firm value.
6. Firm size has a significant and positive effect on firm value.
7. Earnings management does not moderate the relationship between good corporate governance (institutional ownership, independent commissioners and audit committees), profitability, financial leverage, and firm size as related to firm value.

Limitation

This research has the following limitations:
1. Low supervision of the company results in a lack of control by external parties so that institutional ownership is not a factor that can affect firm value.
2. The presence of the audit committee has proven unable to increase firm value, even though the results of the study indicate that the audit committee influences firm value. In this study, proven earnings management is not a moderating variable that can strengthen or weaken the relationship between good corporate governance (institutional ownership, independent commissioners and audit committees), profitability, financial leverage and firm size on firm value.

Suggestion

Based on the conclusions and limitations of the research above, the researcher recommends the following.

For future researchers:
1. It is necessary to test other factors of good corporate governance, instead of institutional ownership, such as audit quality that can increase supervision and affect firm value.
2. Need to test factors related to the audit committee, such as the effectiveness of the number and role and responsibilities of the audit committee so that firm value can increase.

3. Need to test factors other than earnings management, such as cash flow from operations (CFO) or cost of goods sold (COGS), used as moderating variables to moderate the relationship between good corporate governance (institutional ownership, independent commissioners and audit committees), profitability, financial leverage and firm size on firm value.

For companies:

Based on the factors that influence high or low firm value, the company can improve the quality of internal control, especially in risk management where managers (the principal) consider supervision in every business activity of the company (Akhmetshin et al., 2019). One internal control tool that companies can use is Enterprise Risk Management (ERM) issued by COSO as an international management standard (COSO, 2017).

For shareholders:

Shareholders must be more careful and thorough in assessing company performance. In addition to attending to good corporate governance, shareholders can analyse other factors, namely Corporate Social Responsibility (CSR), in assessing the extent to which companies are responsible for maximising shareholder welfare.

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